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DE RUEHAK #1222/01 1891434  
ZNR UUUUU ZZH  
R 071434Z JUL 08  
FM AMEMBASSY ANKARA  
TO RUEHC/SECSTATE WASHDC 6769  
INFO RUCNCIS/CIS COLLECTIVE  
RUEHZL/EUROPEAN POLITICAL COLLECTIVE  
RUEHGB/AMEMBASSY BAGHDAD 1263  
RUEHIT/AMCONSUL ISTANBUL 4439  
RUEUITH/ODC ANKARA TU  
RUEAIIA/CIA WASHDC  
RHEHAAA/NSC WASHDC  
RUCPDOG/DEPT OF COMMERCE WASHDC  
RHEBAAA/DEPT OF ENERGY WASHINGTON DC

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SENSITIVE  
SIPDIS

EEB FOR A/S SULLIVAN  
SPECIAL ENVOY FOR EURASIAN ENERGY GRAY  
EEB FOR ENERGY COORDINATOR MANN  
EUR FOR DAS BRYZA

E.O. 12958: N/A  
TAGS: [ENRG](#) [EPET](#) [TU](#)  
SUBJECT: SCENESETTER FOR C. BOYDEN GRAY'S JULY 10-13 VISIT  
TO TURKEY

REF: A. ANKARA 1070  
[B](#). ANKARA 1085  
[C](#). ANKARA 1172

[1](#). (SBU) Summary. Your visit coincides with political uncertainty surrounding the fate of the ruling Justice and Development Party (AKP) due to a closure case against it pending in the Constitutional Court. Recent high-profile detentions in connection with a year-long investigation into suspected anti-government plotting have fueled a crisis atmosphere in Ankara. The Turkish government is working hard to project a business-as-usual image and welcomes your visit. Despite the charged political atmosphere, you will have an opportunity to reaffirm our commitment to working with Turkey to further our shared energy goals. Becoming a large-scale, reliable gas transit hub to Europe will bring many benefits to Turkey including the development of resources for Turkey itself; more revenues from gas transit and closer ties to Europe and Central Asia. Turkey supports Nabucco, the gas line to Greece and Italy, and the development of Iraqi gas resources and means to bring them to market. Your visit will be a key step in our engagement of Ankara on the policy choices and practical steps to realize these efforts.

#### Background on Energy Cooperation

[2](#). (SBU) Our cooperation with Turkey on energy issues has a long history. In the 1990s, the U.S. worked with Georgia, Azerbaijan and Turkey to bring about the first and only major non-Russian route for Caspian oil to world markets, the Baku-Tbilisi-Ceyhan pipeline that was inaugurated almost exactly two years ago. More recently, our work with Turkey has been guided by the Shared Vision agreed upon by Secretary Rice and then Foreign Minister Gul in June 2006 that reaffirms our strategic partnership and determination to work together on common challenges and opportunities. Specifically on energy, the Shared Vision commits both sides to work together to "enhance energy security through the diversification of routes and sources, including from the Caspian basin."

#### Growing Domestic Energy Demand

[3](#). (SBU) Rising domestic energy demand makes energy supply security a top Turkish foreign policy goal. On average,

Turkey's energy demand has grown by 8 percent per year. Demand for natural gas grows even faster at 15 percent per year as the government continues the country's transition from dirty coal to cleaner gas usage. By 2020, Turkey will be 18 billion cubic meters (bcm) short of its gas needs, and its supply predicament becomes more dire if contracts with Russia and Algeria are not renewed. A key issue for Turkey is striking the right balance between satisfying its domestic gas needs and its strategic interests in developing a gas corridor to Europe.

#### Coming to Agreement with Azerbaijan

14. (SBU) Thus far, Turkey's negotiating strategy had been to link its need for domestic gas with tariff arrangements for gas transiting Turkey to Europe. We and other European countries have been telling Turkey this strategy will not work. There is some evidence that Turkish leaders may now be understanding this. They have been in high-level discussions with Azerbaijan and SOCAR for a bilateral contract that would go a long way toward meeting Turkey's domestic gas needs. We should urge Turkey to make these negotiations and coming to closure on realistic gas transit arrangements its top priorities.

15. (SBU) To come to an agreement, Turkey and Azerbaijan will need to agree on the quantity of gas to be sold by Azerbaijan and also the price. Of the two issues, the two sides seem closer on volumes (SOCAR willing to offer 5 bcm, and Turkey seeking 8 bcm). Turkey maintains that it wants a "good price" from Azerbaijan that reflects its close location to the source. The GOT's idea of a good price varies. Some say

a price below the Gazprom price (roughly USD 400/tcm) while others believe the price should be below the Baumgarten price (roughly USD 350/tcm).

16. (SBU) Some Shah Deniz consortium members believe that the price that emerges from the Shah Deniz Phase I (SD I) re-negotiations will also be the price for Shah Deniz Phase II gas. The price renegotiation will be difficult for Turkey. Turkish Economy Minister Simsek has estimated that a USD 1 dollar increase in oil prices has a USD 350 million impact on the Turkish budget. The market price for gas is now 3 to 4 times the contract price for SD I gas. Implementing such a steep price increase would be a considerable political risk for the GOT. Previous BOTAS management has faced criminal prosecution for agreeing to price increases much less dramatic. Some sources tell us SD I price renegotiation is likely to go to arbitration which would be a long, drawn out process.

#### Nabucco

17. (SBU) Turkey appointed a coordinator to lead negotiations with Nabucco companies, partner countries and the EU, Osman Goksel. There have been a series of discussions with working-level EU counterparts following the February 2008 visit of EU Nabucco Coordinator Jozias van Aartsen to Ankara, van Aartsen's failure to come back to Ankara has hurt these efforts. Turkish authorities have drafted a timeline and schedule for negotiating the various commercial and intergovernmental agreements that will have to underpin Nabucco, showing a renewed determination and focus on the details of realizing this project. The GOT has also re-organized and re-focused its efforts on Nabucco by bringing in the Foreign Ministry to play a coordinating role for the interagency. On July 1, PM Erdogan announced that Turkey will be ready to sign an Intergovernmental Agreement (IGA) for Nabucco in a few months.

18. (SBU) An important topic for EU-Turkey negotiations on Nabucco has been strategizing on ways to bring Turkmen and Kazakh gas to the project. Turkey would like to play a supporting role in bringing these new gas resources to Europe and would like to use the opportunity to develop a commercial

gas hub in Turkey. It understands that these additional resources are necessary for the viability of proposed infrastructure projects, European gas supply security, and the Central Asians' real independence from Moscow. Turkey believes the hub would increase the competitiveness and transparency of Europe's gas market by establishing an open trading platform where any company could buy or sell gas. Spot trading at the hub would be in addition to, rather than in place of, long-term supply and transit contracts.

#### Iraq

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¶9. (SBU) Turkey is interested in helping Iraq develop its oil and gas sectors but waits like everyone for the passage of hydrocarbon legislation. It would like to see U.S. and Turkish firms partner in Iraq. At the April meeting of the bilateral U.S.-Turkey Economic Partnership Commission, Turkey offered to host, with U.S. support, an investment conference for Iraq in Istanbul that it hopes will take place late this year or in 2009.

¶10. (SBU) Turks understand that Iraqi gas could make an important contribution to the commercial viability of Nabucco. To get this gas to market, they have proposed a new gas pipeline to follow the route of the existing Kirkuk-Ceyhan oil pipeline. To make this route economically feasible, it should be linked to the development of new gas fields in Iraq, which require the passage of the hydrocarbon law. The EU has proposed moving early Iraqi gas via the Arab Gas pipeline through Syria. This line is almost built and may provide the cheapest, fastest and most practical route to market. There are, however, other claimants on Iraqi gas, and inadequate cooperation among the Europeans and Turkey could lose these assets to other buyers.

#### Iran

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¶11. (SBU) Turkey's relationship with Iran is multidimensional. The GOT has supported and assures us it is implementing the Security Council resolutions sanctioning Iran, and has recently urged Tehran to seriously consider the latest P-5 1 offer. On the other hand, it also continues to discuss energy cooperation with Iran, mesmerized by that country's resources and determined not to be left out as others make deals with Tehran. A bilateral MOU concluded nearly a year ago contemplates Turkish-Iran cooperation to develop a block in the South Pars gas field and build a dedicated pipeline to Turkey. To do this, Turkey will need partners both for financing and technical expertise. Negotiations have been proceeding slowly at the technical level. Turkey knows from experience that Iran is a difficult and unreliable business partner. Turkey currently imports 6.2 bcm from Iran annually, roughly 17% of its total gas usage. Iran has cut off supplies for the past several winters and left Turkey paying high spot market prices for LNG to meet demand. Your visit is an opportunity to remind Turkey that doing business with Iran is risky, brings little reward and is against US policy and law.

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WILSON